Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
Universal Service Contribution Methodology	)	WC Docket No. 06-122
A National Broadband Plan For Our Future	)	GN Docket No. 09-51

COMMENTS OF XO COMMUNICATIONS SERVICES, LLC.

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SUMMARY

XO commends the Commission for launching this comprehensive review of the federal universal service fund ("USF") contribution system. The 15-year old universal service system is showing the signs of stress. The USF contribution factor, which has averaged 17.0 percent over the first three quarters of 2012, is too high to be sustainable, and has been trending higher due to program demand increases and a steady decline in the current assessable revenue base. Beyond the high contribution factors, the process for resolving USF appeals has broken down, new technologies have challenged revenue allocation rules, and the Form 499-A Instructions have erroneously become *de facto* FCC rules. Now is the time for the FCC to act to modify the USF contributions methodology and address the flaws that make administration of USF contributions burdensome for contributors, the telecommunications industry and end users. XO recommends action in five areas.

First, regardless of the contribution system that will apply in the future, the Commission should take several immediate, interim steps to address flaws in USF contributions today. The Commission should resolve the backlog of USF appeals and guidance requests before the FCC, many of which have been pending for years. The industry needs this guidance promptly, to promote consistency in USF application and to guide the industry through any transition period to new rules. The Commission should adopt rules for the reporting of telecommunications revenues received from MPLS-enabled services, move immediately to an annual contribution factor and end the unfair asymmetrical revisions deadline for modifications to Form 499-A revenue reports. These actions should be taken in advance of final action on the *FNPRM*'s proposals to promote the stability and fairness of the Universal Service Fund.

Second, XO supports the continued use of revenues as the basis for USF contributions. The Commission can best stabilize the funding base for universal service and minimize administrative burdens on contributors and end users through the use of a revenues-based contribution system. As the Commission found in 1997, end user revenues remain the most simple and fairest basis on which to establish an "equitable and non-discriminatory" allocation of the burden to support universal service. Other proposed methodologies for assessing USF contributions would require complex new line-drawing, would require the development of new tracking systems and audit capabilities and would not ensure that providers of interstate telecommunications services make equitable and nondiscriminatory contributions to USF, as required by 47 U.S.C. § 254.

The problems with the current revenues-based system are best addressed by broadening the revenue base for contributions. Since the USF program was established, the telecommunications market has evolved significantly. The current system is under stress because end users have migrated from historically assessable services to new types of services that are not currently assessable. The Commission should respond to changes in technology and the marketplace by updating its list of services that are subject to USF assessments, thereby ensuring that all providers of telecommunications used by today's end users make an equitable and non-discriminatory contribution toward support of universal service. Such changes are well within the Commission's statutory authority and can establish a stable foundation for the Fund for years to come.

Third, XO offers suggestions for increasing the efficiency and predictability of USF administration under any contribution methodology. Despite legitimate concern that USAC is applying the Form 499-A Instructions as rules rather than guidance, the Commission should not respond by imbuing the Instructions with the force of rules. Any attempt to distill FCC Orders into concise binding Instructions either would fail to capture the history and nuance of carefully-balanced FCC decisions or the entire process would rapidly become a quagmire as interested parties re-fight battles decided in separate proceedings. Apart from the Instructions, XO supports the use of an annual USF contribution factor under any contribution system, opposes the proposed "pay and dispute" policy, and proposes changes to USF audits and FCC appeals to make the process more fair and efficient.

Finally, XO opposes further administrative burdens on a telecommunications carriers' recovery of USF contribution obligations from end users. There is no legal basis for prohibiting service providers from identifying USF contribution recovery charges in a truthful and non-misleading line-item on customer invoices. There also is no need for burdensome "trust funds" in order to address what is in comparison an extremely minor problem in USF recovery due to contributor bankruptcy proceedings. Both proposals should be rejected.

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XO Communications Services, LLC and its affiliates (collectively, "XO") by its attorneys, hereby files these Comments on proposals to reform the federal universal service fund contribution system.[1] For the reasons explained below, XO urges the Commission to act expeditiously to fix the many problems plaguing the current contribution system and to broaden the revenue base for contributions in order to stabilize funding and more equitably distribute the contribution obligations.

In these Comments, XO responds to the Commission's request for comments on all aspects of the contribution system. First, XO recommends immediate actions the Commission should take, in advance of final action on the *FNPRM*'s proposals and regardless of the contribution methodology ultimately selected, to address vexing problems with the current system. Second, XO supports the continued use of revenues as the basis for USF contributions and recommends ways to broaden and more fairly distribute the contribution obligation. Third,

1 *Universal Service Contribution Methodology; A National Broadband Plan for our Future*, Further Notice of Proposed Rulemaking, WC Docket No. 06-122, GN Docket No. 09-51, FCC12-46 (rel. April 30, 2012) ("*FNPRM*").

XO explains why a revenues-based contribution methodology is preferable and more administratively simple than a numbers-based, connections-based or hybrid methodology. Fourth, XO offers suggestions for increasing the efficiency and predictability of USF administration under any contribution methodology. Finally, XO opposes further administrative burdens on a telecommunications carriers' recovery of USF contribution obligations from end users.

I. <u>BACKGROUND</u>

XO is one of the largest facilities-based competitive providers of telecommunications and information services in the country. XO delivers a comprehensive array of telecommunications solutions to growing businesses, large enterprises, government customers, information service providers, and other telecommunications carriers.

XO markets communications solutions to government agencies and business customers ranging in size from small businesses to Fortune 500 companies. XO offers these customers IT infrastructure, managed IP, data and end-to-end voice communications services. These services include point-to-point dedicated circuits providing a variety of capacities and utilizing a variety of transmission technologies and capabilities. In addition, XO offers Internet access, VoIP and managed IP services such as IP-VPN, Virtual Private Line Services ("VPLS") and Multi-Transport Network Services ("MTNS").

XO delivers a broad range of IP, data and wholesale voice services to local exchange carriers, interexchange carriers, other telecommunications service providers and information service providers ("ISPs"). XO offers customers high-capacity metro and intercity dedicated transport circuits, along with wholesale voice and data origination and termination services. As a result, XO has a large base of reseller customers that purchase service for incorporation into their own end user services.

XO has extensive experience with the requirements and difficulties of the present contribution system. XO reports revenue on most of the 20 assessable revenue lines, the 15 non-assessable wholesale revenue lines and the four non-telecommunications lines of the Form 499-A. The Company developed a comprehensive system to painstakingly map each service offered to one of these lines and to identify a methodology for performing jurisdictional allocations for each service offered. It also has in place policies and procedures to obtain annual certifications from its base of over 350 reseller customers and to map revenue from each reseller to an appropriate wholesale or retail line on the Form 499-A.

XO also has significant experience with the audit and review processes employed by the universal service administrator, the Universal Service Administrative Company ("USAC"). Over a two year period, USAC conducted an extensive audit of the revenues reported by XO on its 2008 FCC Form 499-A. Ultimately, the audit consumed thousands of person hours within XO, and likely many hundreds within USAC as well. The Audit Report itself is 195 pages long, and includes eight proposed audit findings and two "other matters." Both "other matters" in the Audit Report are associated with pending guidance requests before the Commission. XO submitted a Request for Review of the USAC decision on December 29, 2010. Commenters supported XO's argument that USAC had misapplied FCC rules in reallocating revenue to increase XO' USF contribution obligations.[2]

As such, XO is pleased to offer these comments on the Further Notice of Proposed Rulemaking in this docket. The Commission's FNRPM is thorough and detailed. It

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2 *See* Reply Comments of XO Communications Services, Inc., at 2-5, WC Docket 06-122 (filed Feb. 22, 2011).

outlines the most significant problems facing the contribution system today, and proposes a variety of alternatives for addressing these problems and stabilizing the USF contribution system. XO commends the Commission for undertaking this comprehensive review. We urge the Commission to place equal emphasis on examining the issues raised in this docket expeditiously.

II. REGARDLESS OF WHICH CONTRIBUTION METHODOLOGY IS CHOSEN PROSPECTIVELY, THE COMMISSION MUST TAKE IMMEDIATE STEPS TO ADDRESS FLAWS IN THE CURRENT SYSTEM

The nearly 200-page length of the *FNPRM* underscores the magnitude of the task before the Commission. In the *FNPRM*, the FCC seeks comment on the definition, legal authority, operation and implementation of three fundamentally different ways of assessing USF contributions – revenues-based, numbers-based or connections-based methodologies.[3] These alternatives likely will generate significant comment and will require careful review of hundreds of proposals for modification of one or another of the alternatives. If the Commission adopts a new contribution system, it also promises a reasonable transition period for the industry to implement the system.[4]

Thus, it is apparent that the Commission has a significant task before it, and that it potentially has a complex transition to manage in the near future. It is equally apparent – and recognized in the separate Commissioners' statements[5] – that the need for reform of the current system is urgent. XO submits that certain reforms should not await the Commission's final consideration of a prospective contribution methodology. The Commission can and should act in

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3 *FNPRM* at ¶¶ 98-341.

4 *FNPRM* at ¶ 26.

5 *See* Separate Statement of Commissioner McDowell (contribution reform is "a vital cornerstone" to USF reform); Separate Statement of Commissioner Clyburn (agreeing with "consistent calls" for the Commission to address contribution reform).

targeted areas to address significant problems with the current contribution system. These problems will persist at least through the evaluation of alternative systems and though an implementation period if a major revision is adopted. The reforms below are needed now.

A. <u>Decide Backlog Of Pending Appeals And The Pending Guidance Requests.</u>

The *FNPRM* notes that, "The contribution system has become increasingly complex for the Commission and [USAC] to administer and burdensome for contributing telecommunications providers to comply with."[6] The current revenues-based methodology involves myriad service distinctions, classification issues, jurisdictional allocations and apportionment of revenues for bundled services. Not surprisingly, a number of issues have arisen about how to apply these distinctions in specific contexts. Lack of guidance on these issues complicates USF reporting and exposes carriers to excessive uncertainties.

US Telecom's recent *ex parte* identifies nine appeals and one application for review that remain pending on a variety of critical USF issues.[7] In addition to these substantive appeals, a handful of appeals address other issues in USF administration.[8] USAC also has submitted three formal guidance requests addressing ambiguities in the Form 499-A Instructions.[9] Many of these requests have been pending for years with no action.

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6 *FNRPM* at ¶ 4.

7 Letter from David B. Cohen, USTelecom, to Marlene H. Dortch, FCC, WC Docket No. 06-122 *et al.* (filed Mar. 28, 2012) (*USTelecom ex parte*).

8 *See, e.g., Request for Review by InComm Solutions, Inc. of Decision of Universal Service Administrator*, Request for Review and Petition for Waiver, WC Docket No. 06-122 (filed Feb. 6, 2012) (credit for payments made to wholesale carrier); Level 3 Application for Review, WC Docket No. 06-122 (filed Mar. 1, 2010) (seeking review of decision applying late fees, penalties and interest to late-filed Form 499-A); Ascent Media Group, Inc., Petition for Reconsideration, WC Docket 06-122 (filed Jan. 14, 2009) (seeking review of decision applying late fees, penalties and interest to late-filed revision to Form 499-A).

9 Universal Service Administrative Company, Guidance Request, WC Docket No. 06-122 (filed Apr. 22, 2011) (reporting of text messaging revenues); Universal Service Administrative Company, Guidance Request, WC Docket No. 06-122 (filed Mar. 1,

The FCC should decide as many of these appeals as it can, as quickly as it can. The pendency of the *FNPRM* – which addresses prospective rules or modifications of the system – does not alleviate the need for clarity as to the existing rules. These appeals and guidance requests involve issues with industry-wide significance (the identification of wholesale revenues, classification issues, etc.), many of which have arisen in multiple appeals. For example, reseller certification questions had been raised in at least six appeals prior to XO's December 2010 appeal. Private line jurisdictional allocation issues were raised in an appeal two years before XO's appeal,[10] and again were raised in at least one subsequent appeal.[11] The industry needs guidance on these issues in order to prevent their recurrence and to promote uniformity in the application of USF contribution obligations now and during any potential transition period.

Moreover, the pending appeals involve specific amounts claimed to be owed to the Fund. Petitioners generally either pay the disputed amounts into the Fund or hold a reserve for possible liability depending upon the resolution of the appeal. In either event, delay in resolution of the appeal effects a financial hardship on the petitioner. The Commission should endeavor to clear this backlog of appeals and guidance requests as soon as possible.

2011) (treatment of certain reseller certifications); Universal Service Administrative Company, Guidance Request, WC Docket No. 06-122 (filed Aug. 19, 2009) (prepaid card revenue reporting, classification of ATM/Frame Relay, classification of IP-VPN, and other issues).

10 *Request for Review by Madison River Communications, LLC of Decision of Universal Service Administrator*, Request for Review, WC Docket No. 06-122 (filed Dec. 12, 2008) ("Madison River Request for Review"); *see XO Communications Services, Inc. Request for Review of Decision of the Universal Service Administrator*, Request for Review of Decision of the Universal Service Administrator, WC Docket No. 06-122 (filed Dec. 29, 2010) ("XOCS Request for Review");

11 *Request for Review of PaeTec Communications, Inc. of Universal Service Administrator Decision*, Request for Review of PaeTec Communications, Inc. of Universal service Administrator Decision, WC Docket No. 06-122 (filed April 3, 2012) ("PaeTec Request for Review").

B. Clarify And Simplify Wholesale Carrier Obligations.

In the *FNPRM*, the Commission seeks comment on two prospective changes to the apportionment of USF obligations between wholesale telecommunications providers and their reseller customers.[12] In addition to these prospective changes, the Commission expresses an intent to address pending appeals involving wholesale carrier obligations.[13] XO supports prompt action on these pending appeals.

The contribution obligations of wholesale carriers and their customers have been raised repeatedly in USF appeals. XO's own appeal was but an iteration of a question repeatedly raised in USF appeals before the FCC, namely the standard that wholesale carriers must satisfy in order to classify revenues as reseller revenue in block 300 of the Form 499-A. The Wireline Competition Bureau addressed this question in orders issued in 2009[14] and in 2010.[15] However, these orders have not modified USAC's approach to reseller certifications, and the issues have continued to recur.

XO's experience is consistent with the experiences reported by many other wholesale carriers. USAC has been applying an increasingly unrealistic standard for the classification of revenues as "carrier's carrier" revenues. The resulting rigidity with which USAC approaches the issue has imposed on wholesale carriers a virtually insurmountable burden to support their classifications of revenues and has undermined the predictability of the USF

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12 *FNPRM* at ¶¶ 143-78 (discussing a value-added contribution methodology and revisions to reseller certifications).

13 *Id.* at ¶ 145.

14 *Request for Review of Decision of the Universal Service Administrator by Global Crossing Bandwidth, Inc.*, Order, 24 FCC Rcd 10824 (2009) ("Global Crossing Order"), *application for review pending* (filed Sept. 16, 2009).

15 *In re Universal Service Contribution Methodology; Request for Review of Decision of the Universal Service Administrator by Network Enhanced Telecom, LLP*, DA 10-2005 (WCB Oct. 19, 2010) ("NetworkIP Order").

contribution mechanism. Further action is needed to restore the allocation of responsibility between wholesale and retail providers that was established in the *Universal Service Orders*.[16]

XO urges the Commission to provide three needed clarifications immediately. First, the FCC should reconfirm that filer compliance with the Form 499-A Instructions is not mandatory to meet the "reasonable expectation" standard. Specifically, wholesale carriers may classify a customer as a reseller after reliance on the verification procedures in the Instructions <u>or</u> based on "other reliable proof" of a customer's reseller status. Second, the FCC should clarify what information is necessary to establish a "reasonable expectation." A wholesale carrier should be able to rely upon the customer's representations as well as the services that it purchases or indicia of carrier-to-carrier interconnection to establish the reseller's status. Finally, the FCC should make clear that a wholesale carrier will not be made a guarantor for its resellers' non-compliance with the Commission's rules and, conversely, that USF will not be recovered twice, once from the reseller and once from the wholesale carrier, when a wholesale carrier's procedures technically deviate from a safe harbor established in the Instructions but the evidence confirms the reseller has made USF contributions.

C. <u>Adopt The MPLS Industry Group Proposal For Reporting Of Enterprise Revenues.</u>

As the Commission is aware, uncertainty has existed in the industry for many years regarding whether MPLS-enabled services are assessable for USF purposes and, if so, how assessable revenues are to be allocated. XO participated in months of industry discussion and analysis among a diverse group of communications service providers (the MPLS Industry Group) to develop a consistent and competitively-neutral methodology to apply prospectively to

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16 *Federal-State Joint Board On Universal Service*, 12 FCC Rcd 8776, ¶¶ 844, 846-847 (1997).

MPLS-enabled services within the current revenues-based contribution system. XO urges the Commission to adopt this proposal in the interim while it considers additional reforms in order to stabilize a growing component of the USF contribution base and allow the Commission to better evaluate the long-term viability of the revenues-based system.[17] Furthermore, if the Commission maintains the revenues-based methodology, as XO advocates below, adoption of this proposal would provide a fitting transition to broaden the base of assessable revenues by achieving each of the Commission's goals of efficiency, fairness, and sustainability of the Fund.[18]

Under the MPLS Industry Group proposal, revenues associated with the access transmission components of all MPLS-enabled services would be imputed on a uniform basis and made subject to USF contribution obligations by all providers.[19] Providers would contribute based on industry-wide revenue proxies established by the Commission. These revenue proxies, called an "MPLS Assessable Revenue Component" or "MARC," would be set for each designated band of transmission speeds associated with an assessable component. The MARC would be calculated using the NECA Tariff access rates for Rate Band 1 since those rates are publicly available and associated with the largest and most cost-efficient NECA companies.

The MARC proxies would operate as a safe harbor floor for contributions. That is, each provider would report *at least* this amount as assessable interstate telecommunications revenue. Providers could elect to determine the USF contribution base for their MPLS-enabled services using their own access transmission rates *provided that* those rates yield a larger USF

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17 *See* Letter from MPLS Industry Group, to Marlene H. Dortch, Secretary, FCC, WC Docket No. 06-122, at 4-7 (filed Mar. 29, 2012) (describing the industry proposal) ("MPLS Industry Group Letter").

18 *FNPRM* at ¶ 22.

19 MPLS Industry Group Letter at 4-6.

contribution base than the corresponding MARC proxies.[20] Use of uniform revenue proxies would reduce customer confusion by establishing transparent and reasonable safe harbors and ensure competitive neutrality where all providers assess at least the same level of USF on comparable transmission components regardless of their individual pricing strategies for integrated MPLS-enabled services. Additionally, the Commission would have more assurance regarding the contribution base regardless of trends in the marketplace or the classification of various new services.

Importantly, the MPLS Industry Group supports the MARC proxies for prospective assessments of USF contribution obligations. The treatment of MPLS-enabled services requires an industry-wide rulemaking, such as this proceeding, to accomplish. Well-established precedent demonstrates that such rulemaking changes can apply only prospectively.[21] Moreover, prospective resolution of MPLS-enabled service reporting obligations is sound policy. Prospective adoption of the above methodology would avoid the massive, industry-wide disruptions that would likely result from any attempt to impose retroactive uniformity on the varying approaches that service providers adopted in good faith in the absence of guidance from the FCC.[22] Retroactive assessments would create an administrative nightmare for providers and their customers alike (many of whom were, in turn, contributing resellers that made their own good faith assessments of the reporting obligations of the service). Given the passage of time and the myriad of approaches, retroactive contribution obligations would require the Commission and USAC to monitor a massive, lengthy and complex redistribution of USF contributions that would certainly detract from efforts to reform the USF contribution system as

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[20] MPLS Industry Group Letter at 5.

[21] *See Bowen v. Georgetown University Hospital*, 488 U.S. 204 (1988).

[22] MPLS Industry Group Letter at 14-15.

contemplated. Prompt, prospective adoption of the MPLS Industry Group approach will move the reform forward, without unfairly punishing providers of their customers for actions taken in an uncertain environment.

D. <u>The Commission Should Move Immediately To An Annual Contribution Factor While Maintaining Quarterly Revenue Projections For Billing Purposes.</u>

The *FNPRM* discusses a proposal to move to an annual contribution factor instead of a quarterly factor.[23] This proposal has merit, and should be adopted immediately, effective with contributions for charges on or after January 1, 2013. This will simplify billing and recovery of USF contribution payments from end users and make contribution obligations more predictable.

As the *FNPRM* notes, the current quarterly contribution factor is volatile. In the last 12 quarters alone (since 4Q 2009), the USF contribution factor has been revised up or down by at least one full percentage point 6 times.[24] The quarterly contribution factor is only announced approximately two weeks before it goes into effect,[25] which leaves carriers with little time to implement the necessary changes to their billing systems to apply the current contribution factor.

These quarterly changes are affected not only by past period adjustments, as the *FNPRM* notes, but also by seasonality in USF contribution revenues. Despite a general decline

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23 *FNPRM* at ¶ 353.

24 *See* http://www.fcc.gov/encyclopedia/contribution-factor-quarterly-filings-universal-service-fund-usf-management-support; s*ee also, FNPRM* at ¶ 358 (USF contribution factor increased or decreased by more than one percentage point 11 times between 1Q 2005 and 2Q 2011).

25 *See, e.g., Public Notice, Proposed Third Quarter2012 Universal Service Contribution Factor*, DA 12-917 (rel. June 11 2012). This Public Notice was released 20 days before the factor took effect. By its terms, the Public Notice did not become final until June 25. *Id.* at 4; *see* 47 C.F.R. § 54.709(a)(3) (providing a 14-day period for the Commission to modify the proposed factor before it is deemed approved).

in assessable revenues, the revenues continue to vary significantly by quarter. Revenues tend to be lower in the second quarter of the year, and to increase significantly in the third quarter.[26] This is not too surprising, given that toll revenues have long been recognized to be seasonal.[27] Moving to an annual factor will eliminate this seasonality effect on the rates.

By contrast, the Commission has experience with an annual factor in the assessment and collection of other funds, such as TRS, NANPA and FCC Regulatory Fees. In these cases, the annual contribution factors have been relatively stable, and certainly do not exhibit the volatility shown in the quarterly USF factor.

However, carriers should continue to project revenues to USAC on a quarterly basis. These quarterly projections are used to send monthly USF invoices, which in turn are subject to an annual true-up based on the Form 499-A. These quarterly projections are more accurate than would be annual projections. As a result, retention of the Form 499-Q quarterly projections will minimize the magnitude of true-ups as a result of the Form 499-A annual revenue filings.

E. <u>The Commission Should Adopt A Single, Reciprocal Limitations Period For Adjustments To Reported Revenue.</u>

As the *FNPRM* notes, in 2004, the Wireline Competition Bureau adopted an order that requires contributors to revise their Form 499-A filings within one year if the revision would

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26 *See*, FCC, *Universal Service Monitoring Report: 2011*, CC Docket No. 98-202, Table 1.9 at n.7 (listing quarterly USF contribution bases) ("*2011 USF Monitoring Report*").

27 *See, e.g., Virgin Islands Tel. Co. v. FCC*, 989 F.2d 1231 (D.C. Cir. 1993) (two year monitoring period used by FCC "minimizes the impact of seasonal 'peak' and 'valley' earnings periods"); *Connect America Fund, et al.*, Report and Order and Further Notice of Proposed Rulemaking, WC Docket Nos. 10-90 *et al.*, FCC 11-161, ¶ 549 (rel. Nov. 18, 2011) (adopting rule allowing the FCC to instruct USAC how to handle excess contributions in order to "better manage one-time and seasonal events that may create undue volatility in the contribution factor").

result in a decrease in the contributor's contribution obligation.[28] This order is the subject of three pending Applications for Review filed by SBC Communications, Inc. ("AT&T"), Qwest Communications International, Inc. ("Qwest"), and Business Discount Plan, Inc. ("BDP"), each of which was filed on January 10, 2005. These Applications for Review have been pending for far too long. The Commission should act now to resolve the applications and to establish a reasonable, *reciprocal* deadline for revisions to revenues reported on the Form 499-A.

As shown in AT&T's Application for Review, the One Year Downward Adjustment Deadline is a substantive rule adopted outside the scope of the Bureau's delegated authority.[29] The Bureau is precluded from making substantive changes to the Form 499-A Instructions. Moreover, the One Year Downward Adjustment Deadline is arbitrary and fundamentally unfair. It is arbitrary for a filer to be precluded from making modifications that would result in a decrease in the filer's contribution obligation if more than one year has passed, when there is not a corresponding time limit for modifications that would increase a filer's contribution base.[30] The purported gains in administrative efficiency, certainty, and integrity of the Commission's contribution system is completely outweighed by the harms resulting from the rule – depriving parties of the ability to make changes in the face of the incredible complexity of the contribution rules. More than one year often is necessary to examine adequately the legal classifications and difficult technical distinctions underlying the rules.[31]

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28 *Federal-State Joint Board on Universal Service et al.*, Order, 20 FCC Rcd 1012, 1013 (WCB 2004), *applications for review pending*.

29 Application for Review filed by SBC Communications, Inc. ("AT&T"), CC Docket No. 96-45 *et al.*, at 7-9 (filed Jan. 10, 2005) (*AT&T Application*). *Accord* Application for Review filed by Qwest Communications International, CC Docket No. 96-45 *et al.*, at 7-8 (filed Jan. 10, 2005) (*Qwest Application*). *See In re 1998 Biennial Regulatory Review*, 14 FCC Rcd 16602, 16621 ¶ 39 (1999).

30 AT&T Application at 10-11.

31 Qwest Application at 11-17.

As Qwest noted, under the federal income tax code, the same statute of limitations period applies to both underpayments and overpayments, and the Internal Revenue Code allows netting of overpayments and underpayments for applicable years still open under the statute of limitations.[32] XO supports a similar reciprocal rule for both upward and downward revisions to USF revenue reports. XO believes that a time period of two years for both downward and upward adjustments adequately balances the need for a reasonable time for revisions with the need for certainty within the Fund.

III. LONG TERM REFORM – THE UNIVERSE OF ASSESSABLE SERVICES MUST BE EXPANDED SUBSTANTIALLY TO PRESERVE AN ADEQUATE CONTRIBUTION BASE AND ENSURE COMPETITIVE EQUALITY.

XO supports the continued use of revenues as the basis for USF contributions and recommends ways to broaden and more fairly distribute the contribution obligation as set forth below.

A. Congress Intended that the Burden of Funding USF be Spread Broadly and Shared Equally.

Section 254(d) of the Act requires that "[e]very telecommunications carrier that provides interstate telecommunications services shall contribute" to universal service funding, *and* that the Commission establish mechanisms to ensure that contributions are assessed on an "equitable and nondiscriminatory basis."[33] Moreover, the Commission is empowered to require "[a]ny other provider of interstate telecommunications" to participate in universal service funding "if the public interest so requires."[34] The clear intention of Congress was to spread the burden of contributing to universal service subsidy support broadly, both to ensure that the

32 Qwest Application at 17, *citing* 5 U.S.C. §§ 6402 and 6501.

33 47 U.S.C. § 254(d).

34 *Id.*

contribution base is sufficiently large to provide funding adequate to achieve the purposes of the universal service fund program *and* to avoid unfairly burdening any particular set of services or service providers.

Consistent with this Congressional intent, the Commission has three goals when establishing mechanisms for universal service support – namely, ensuring the stability and sufficiency of the universal service fund, providing that contributors be assessed in an equitable and nondiscriminatory manner, and minimizing the regulatory costs of complying with universal service obligations.[35] The need to spread the contribution burden as broadly as reasonably possible is fundamental to ensuring that the telecommunications market is not artificially distorted by saddling one set of telecommunications services with hefty universal service funding obligations while conferring an artificial regulatory advantage on competing services that are not required to provide universal service support. From the outset, the Commission held that universal service contribution mechanisms must be competitively neutral and "neither unfairly advantage or disadvantage one provider over another, and neither unfairly favor nor disfavor one technology over another."[36]

Accordingly, the Commission has used its permissive authority under Section 254(d) to require "other provider[s] of interstate telecommunications" to contribute to universal service support whenever it is determined that they benefit from access to the subsidized public switched telephone network ("PSTN").[37] As early as 1997, the Commission exercised its

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35 *Federal-State Joint Board on Universal Service,* CC Docket No. 96-45, Further Notice of Proposed Rulemaking and Order, 17 FCC Rcd 3752, 3759 (2002) (*First Contribution Methodology Order*).

36 *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Report and Order, 12 FCC Rcd 8776, 8801 (1997) (*Universal Service First Report and Order*).

37 *Universal Service First Report and Order*, at 9184-85; *see also*, *Texas Office of Public Utility Counsel v. FCC*, 183 F.3d 393, 428 (5th Cir. 1999) ("Congress designed the

permissive authority to include certain categories of non-telecommunications carriers on the list of required universal service contributors. In adding private carriers and payphone aggregators to the list, the Commission emphasized that it was preserving competitive neutrality by ensuring that no technology gleaned a competitive advantage due to a universal service support exemption, broadening the contribution base to fairly spread the burden of universal service funding between classes of service providers that compete against one another in the marketplace, and carefully extending the obligation only to businesses that include "telecommunications" in the "core" of their business.[38] Much the same rationale was used by the Commission in 2006 to add interconnected VoIP providers to the list of mandatory contributors.[39] Importantly, by treating interconnected VoIP providers as "other providers of telecommunications," the Commission established that providers of enhanced or information services can be required to contribute directly to universal service support when their services incorporate the provision of telecommunications.

B. Market Evolution has Undermined the Commission's Intent to Spread the Universal Service Support Obligation Evenly and Effectively.

When the current universal service program was established in 1997, the telecommunications industry was overwhelmingly composed of wireline telecommunications carriers providing voice services. The use of mobile wireless services have exploded since that time, resulting in reduced use – and, increasingly, displacement – of wireline services. Mobile wireless service is increasingly sold in bundles of voice, text messaging and data services, which

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universal service scheme to exact payments from those companies benefiting from the provision of universal service.")

38 *Universal Service First Report and Order*, 12 FCC Rcd at 9183-84..

39 *Federal-State Joint Board on Universal Service,* CC Docket No. 96-45, Second Contribution Methodology Order, 21 FCC Rcd 7518 (2006) ("*Interconnected VoIP Order"*).

enables wireless carriers to report an increasingly smaller portion of revenue as assessable for universal service purposes under current rules. Similarly, customers are swiftly migrating to broadband connections, often provided by cable companies. Like wireless services, services delivered over such broadband connections are sold as a bundle of voice and Internet access services, enabling service providers to report a substantial portion of revenue as non-assessable for universal service purposes. Even for customers that remain on basic wireline connections, telecommunications carriers increasingly sell services as a bundle of local and interexchange services – often providing virtually unlimited toll calling at fixed rates – making it difficult to accurately separate interstate from intrastate assessable revenues for universal service contribution reporting purposes. Finally, substantial reductions in interstate switched access charges have flowed through into lower interstate toll service rates, greatly reducing the interstate toll service revenue that is subject to USF assessment.

Not surprisingly, these developments have led to a substantial decrease in the base of industry revenue that currently is assessable for federal universal service contributions. At the same time that the demand for universal service support increased from $4.5 billion to $8.1 billion annually, the revenue base for universal service contributions actually declined from $75.8 billion to $67 billion.[40] The decline in the assessable base is *not* attributable to a contraction of the overall telecommunications industry in the United States. Total industry revenue reported by telecommunications carriers actually increased substantially from $335 billion to $444 billion between 2000 and 2010.[41] However, most industry revenue is now earned in service categories that the Commission treats as non-assessable for universal service purposes under current rules. For example, telecommunications service providers report over $158 billion

[40] *See, FNPRM* at ¶ 20.

[41] FCC, *Telecommunications Industry Revenues: 2009*, Table 2.

annually to USAC as non-assessable "Non-Telecommunications" revenue, despite the fact that many (if not most) of the products in the category have telecommunications transmission components embedded in them.[42]

As the telecommunications industry has evolved, service providers (and their customers) have steadily substituted new products that are treated as exempt from federal universal service assessment in place of the legacy interstate voice telephony offerings that remain fully assessable. Consumers have migrated to bundled voice telephony packages where interstate "long distance" minutes ostensibly are offered for substantially reduced (or even "free") prices. They also use mobile wireless phones in place of wireline services, and CMRS providers are obligated to report only a relatively minor portion of the resulting revenue as stemming from assessable interstate telecommunications. And critically, Commission decisions that have classified all broadband Internet access as "information service" greatly exacerbate the problem by assigning this huge growth area to a non-assessable category.

Notably, this product substitution likely is driven at least in part due to the significant artificial cost advantage that non-assessable services have over assessable services – *i.e.* the substantial government imposed fee on assessable services is a powerful incentive for consumers to replace them with less costly non-assessable services. As NTCA has explained, "[s]addling traditional wireline and wireless voice service with the entire USF contribution burden…accelerate[s] the migration away from these services to cheaper alternatives…."[43] Indeed, such product substitution creates a sort of negative feedback loop in which ever higher

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[42] *See,* FCC, *Universal Service Monitoring Report: 2011,* CC Docket No. 98-202, Table 1.2 (*"2011 USF Monitoring Report"*). Notably, this number actually understates the impact, since it does not reflect any revenue of the myriad service providers that take the position that all of their revenue is "non-assessable" enhanced or information service revenue, and thus choose not to register with and report to USAC at all.

[43] Comments of NCTA, WC Docket No. 05-337 (Dec. 22, 2008).

universal service contribution factors cause more customers to substitute non-assessable services, which in turn further reduces the base of assessable revenue and requires the contribution factor be adjusted further upward.

The net result has been a universal service contribution factor that has spiraled out of control. The federal universal service contribution factor has steadily inflated from just under 4% at the program's inception[44] to 15.7 percent today, with highs over 17 percent for both of the first two quarters of 2012.[45] Clearly, the framers of the universal service program never contemplated imposing such a shockingly high "tax" rate on telecommunications services.[46] Apart from the question of whether such a wealth transfer is justifiable at all, the extraordinarily high assessment factor actually is contrary to at least two of the Commission's stated goals for any universal service contribution mechanism. First, as explained above, the extremely high assessment factor actually causes product substitution, which in turn causes the contribution base to contract steadily. Second, such a high assessment rate creates a stark competitive inequality; legacy services are burdened with a huge artificial cost disadvantage in the marketplace.

Thus, the current universal service contribution system is broken and cries out for reform. In XO's view, the situation is sufficiently acute that the best reform is one that can be implemented most easily and quickly. As explained in the next section, XO believes that contribution reform can best be accomplished by retaining the existing system of assessing

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44 Public Notice, First Quarter 1998 Universal Service Contribution Factors Revised and Approved, DA 97-2623 (rel. Dec. 16, 1997) (adopting a total contribution factor of 3.91%).

45 Public Notice, Proposed Third Quarter 2012 Universal Service Contribution Factor, DA 12-917 (rel. June 11, 2012).

46 Although universal service charges are not technically classified as taxation, they are mandatory upon service providers, and have an identical functional impact on both service providers and their customers.

revenues, but substantially expanding the list of services and service providers whose revenues are treated as assessable.

C. **<u>The List of Assessable Services Must be Expanded Substantially to Ensure Viability of the Fund and Spread Support Obligations Fairly Among Competing Service Providers.</u>**

The problem with the current USF contribution system is not the revenues-based assessment *per se*; rather, it is that growth of assessable revenues has not kept pace with the increasing need for USF funding. For example, while the demand for USF funds increased from $5.97 billion in 2004 to a total projected demand of $8.6 billion in 2011 (a 44.1% increase), assessable interstate and international telecommunications revenue actually decreased from approximately $80 billion to a projected total of only approximately $67 billion during the same timeframe (a 16% decrease). Because the funding demand has grown while assessable revenues have declined, the contribution factor has necessarily increased substantially. Indeed, the contribution factor has increased from 8.76% in 2004, for example, to an average rate of 17.0% over the first three quarters of 2012 (a 94.1% increase).[47]

It is key to recognize that telecommunications-related revenue has actually continued to grow. Even a casual observer knows that wireless communications and Internet communications have experienced explosive growth over the past decade. It is only "assessable" revenue that has declined. Relatively modest expansions in the assessable revenue contribution base can quickly result in a substantial reduction in the USF contribution factor and a return to a more equitable apportionment of the obligation to support universal service.

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[47] *See, 2011 Universal Service Monitoring Report,* Table 1.1 & Table 1.2.

1. **The Commission should interpret "provider of interstate telecommunications" broadly**

Section 254(d) of the Act makes all "telecommunications carriers" mandatory contributors to the universal service fund, but permits the Commission to also extend universal service contribution requirements to any "provider of interstate telecommunications" if the "public interest so requires."[48] The Commission's permissive authority is a critical tool that must be used aggressively to preserve and protect the universal service program. The Commission has correctly recognized in prior orders that the term "provide" is broader than "offer."[49] Many companies offer integrated services that combine telecommunications transmission with information services. Such firms "provide" telecommunications as part of their integrated service offering even when they do not "offer" telecommunications transmission separately.[50] As ever more stand-alone telecommunications services are displaced in the marketplace by integrated telecommunications/information services, it is of the utmost importance that the Commission continue to exercise its permissive authority broadly to make all telecommunications transmission subject to universal service fund assessment, whether offered on a stand-alone basis or provided as one component of an integrated service offering.

By the same token, the Commission must remain steadfast in determining that the "public interest…requires" it to compel "provider[s]" of telecommunications to contribute directly to universal service funding whenever such action is necessary to ensure either competitive fairness among service providers or sustainability of the fund. In particular, the Commission must reaffirm that the notion of competitive neutrality requires that companies that are not mandatory contributors, but nonetheless benefit from access to the PSTN, must be

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48 47 U.S.C. § 254(d).

49 *Interconnected VoIP Order*, 21 FCC Rcd at 7539.

50 *See Vonage Holdings v. FCC*, 489 F.3d 1232, 1240-41 (D.C. Cir. 2007).

assessed directly when their integrated service offerings are offered as competitive substitutes for telecommunications services that are subject to universal service assessment.[51] Anything less would unfairly handicap telecommunications carriers by regulatory fiat, and cause them to redesign their products as necessary to discontinue separately offering telecommunications transmission – thereby denying consumers the flexibility to order telecommunications services separately from non-telecommunications services. As importantly, failure to assess telecommunications transmission when included as part of integrated telecommunications/information services offerings would ensure that the assessable revenue base would continue to atrophy, ultimately to a point where the assessment burden on mandatory contributors would be unsustainable.

Notably, the Commission has been correct in addressing universal service contribution obligations on a service-by-service basis.[52] Many service providers offer both stand-alone telecommunications services and integrated telecommunications/information services to their customers, while other service providers have elected to provide only integrated offerings. Whenever service providers offer comparable service offerings, they should be treated equally with respect to universal service funding obligations. A company should not be able to obtain a competitive advantage – and evade universal service support responsibilities – simply by opting to provide integrated services exclusively. Thus, universal service funding obligations should depend on the type of service provided, not the identity or classification of a particular service provider.

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51 *Universal Service First Report and Order*, 12 FCC Rcd at 9173-74.

52 *FNPRM* at ¶¶ 36-37; 47 U.S.C. § 54.706.

2. **<u>The Commission must modernize the universal service contribution mechanism by expanding the list of assessable services</u>**

The universal service contribution framework has failed to keep pace with a telecommunications industry that has quickly migrated from TDM-based wireline voice services to an assortment of wireless and packet-based communications services. The Commission must quickly update its universal service contribution rules by adding services that currently get an undeserved and unfair "free pass" from universal service contribution obligations to the list of services that are assessed universal service contributions directly.

a. **<u>MPLS-enabled and other enterprise communications services</u>**

Given the shift from traditional stand-alone services to integrated enterprise communications services, XO supports the Commission's proposal to impose contribution obligations on those integrated services that have an interstate telecommunications component. As discussed in the context of interim changes to the current revenues-based system, XO urges the Commission to adopt the MPLS Industry Group proposal to resolve prospectively the uncertainty regarding assessment of MPLS-enabled services. XO submits that this proposal could be applied more broadly to other integrated services.

The Commission proposes a rule that would require providers of interstate telecommunications to treat all revenues from integrated services as assessable unless the provider offers the transmission on a stand-alone basis, in which case only the revenues associated with the transmission would be assessable.[53] However, XO believes that adoption of the proxy methodology submitted by the MPLS Industry Group strikes a more appropriate balance by establishing uniform industry-wide proxies for comparable transmission services. The proposal was carefully crafted after considering the various opportunities for providers to

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[53] *FNPRM* at ¶ 117.

undermine their USF contribution obligations, for example by under-valuing their transmission services where their cost structures are more favorable than for other providers. Applying the same assessment methodology more broadly, all providers would treat comparable underlying transmissions similarly for all integrated services, eliminating competitive disadvantages between providers that disparately price their transmission services. Furthermore, adoption of proxies for the assessable revenue of transmission components would simplify administration and enforceability by creating bright line assessable revenue amounts, rather than employing highly-variable provider rates for comparable non-integrated services.

The Commission may exercise its permissive authority to adopt the methodology of the MPLS Industry Group proposal as it applies to MPLS-enabled services or more broadly to all integrated services without determining the regulatory classification of any particular MPLS-enabled or other integrated service.[54] This is particularly beneficial given the variety and growth of service offerings over MPLS networks and decreases the need for Commission intervention to resolve future uncertainties about integrated services, maintaining relevant and applicable contribution rules even as the industry progresses.

b. **Text messaging**

Text messaging via mobile phones, which did not exist when the current universal service contribution rules were crafted, has grown exponentially over the past several years. CTIA estimates that over two *trillion* text messages were sent last year,[55] resulting in approximately $19 *billion* in interstate revenue. While some text messaging undoubtedly is new market growth, it seems self-evident that much texting is simply a substitute for voice

[54] MPLS Industry Group Letter at 9-12.

[55] CTIA, *U.S. Wireless Quick Facts* (Apr. 2012) (available at http://ctia.org/advocacy/research/index.cfm/AID/10323) (last visited July 9, 2012).

communications. Unfortunately, the major CMRS providers take the position that text messaging is an information service which is completely exempt from universal service fund assessment.[56] This position is highly debatable, and other industry participants have asked the Commission to declare that text messaging should be regulated as a Title II service, including the requirement that text messaging be subject to mandatory universal funding assessment.[57] But whatever the correct legal analysis under current rules, it appears that most text messaging revenue is not currently being assessed for universal service support, and USAC has been forced to seek guidance from the Commission on how to treat this gaping – and quickly growing -- loophole.[58]

XO agrees with Public Knowledge's position that text messaging cannot properly be regarded as an information service under current Commission rules and policies.[59] The vast majority of text messages are simple two-way, virtually real time conversations transmitted in textual rather than audio format; importantly, in these conversations, there is none of the net protocol conversion, information storage or data retrieval functionality that normally is required to classify a service as "enhanced." Thus, text messaging is best categorized as a "commercial mobile service" under Section 332 of the Act which in turn is subject to Title II regulation

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56 *See*, AT&T Petition for Immediate Commission Action to Reform Its Universal Service Contribution Methodology, WC Docket No. 06-122, pp. 8-9 (July 10, 2009); CTIA Comments, WC Docket No. 06-122, p. 13 (June 5, 2011); Verizon Wireless Comments, WC Docket No. 06-122 (June 6, 2011).

57 Petition of Public Knowledge for Declaratory Ruling, WC Docket No. 08-7 (Dec. 11, 2007); NTCA Comments, WC Docket No. 06-122 (June 6, 2011)("*Public Knowledge Declaratory Ruling Request*"); Public Knowledge Comments, WC Docket No. 06-122 (June 6, 2011).

58 Letter from Richard A. Belden, USAC, to Julie Veach, FCC Wireline Competition Bureau, WC Docket No. 06-122 (April 26, 2011)("*USAC 2011 Guidance Request*").

59 *Public Knowledge Declaratory Ruling Request*.

(including universal service fund assessment).[60] Depending upon how much text messaging is being reported as assessable today,[61] clarifying that text messaging is subject to mandatory universal assessment would increase the assessable contribution base by more than 25 percent. This one adjustment could materially improve the sustainability of the contribution base, and relieve significant pressure on current contributors by reducing the quarterly contribution factor concomitantly.

However, even if the Commission is not currently inclined to resolve whether text messaging should be regulated as a Title II service, there is no reason to delay adding text messaging to the list of assessable services using its permissive authority. Clearly, text messaging is offered as a substitute for both wireline and wireless voice services, and is fully competitive with those offerings. Thus, assessing texting services is necessary to avoid conferring an artificial and uneconomic regulatory advantage over voice services. In addition, given the sheer volume of texting services, it is evident that making text messaging assessable will materially enhance the sustainability of the universal service funding base. Accordingly, it would make sense to simply make text messaging revenue fully assessable, even under use of permissive authority. Alternatively, if the Commission believes that some portion of text messaging offerings may, indeed, include information service functions, it could permit CMRS providers to report a reasonably allocable portion of text messaging proceeds as assessable revenue. It is apparent that the core of text messaging service is the transmission via telecommunication of packets from the sender to the recipient, so presumably the portion of revenue reasonably allocable to the telecommunications function should be quite high – likely 90

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[60] 47 U.S.C. § 332; *see, Public Knowledge Declaratory Ruling Request*.

[61] USAC indicates in its Guidance Request that at least some CMRS carriers report at least a portion of their text messaging revenue in assessable categories. *See, USAC Guidance Request*.

percent or more.[62] Even with such a reasonable allocation, the addition of text messaging revenue to the universal service would represent a major improvement to the current system.

c. **<u>One-way VoIP services</u>**

The Commission determined six years ago that interconnected VoIP services benefit from access to the PSTN, constitute substitutes for wireline voice telephony, and compete directly with legacy voice telephone services. Accordingly, the Commission correctly exercised its permissive authority to include most interconnected VoIP services to the list services to be assessed for universal service purposes.[63] However, the Commission created a gaping loophole in its definition of assessable interconnected VoIP services by limiting its application to "two-way" communications and omitting so-called "one-way" VoIP services.

One-way interconnected VoIP services benefit from access to the PSTN in the same way that two-way interconnected VoIP services do; *i.e.*, outbound one-way interconnected VoIP is dependent on routing through the PSTN on the terminating end of the call, and inbound one-way interconnected VoIP relies upon use of the PSTN on the originating end of the call. Indeed, the reason that telephone numbers are assigned to customers of these services is to facilitate the routing through the PSTN. Similarly, one-way interconnected VoIP services compete with traditional voice telephony services in the same manner that two-way interconnected VoIP services do. As the Commission observes in the *FNPRM*, Skype itself lists traditional telecommunications carriers as among its primary competitors in its reporting to the SEC.[64] Moreover, the largest one-way VoIP services are provided by tech industry giants

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62 It should be incumbent on CMRS providers to demonstrate that the cost of providing any information service component represents any greater proportion of the cost of service.

63 *Interconnected VoIP Order*, 21 FCC Rcd at 7539; 47 U.S.C. § 54.5.

64 *FNPRM* at n.173.

(Skype is owned by Microsoft and Google provides Google Voice) and have grown to substantial size (Skype alone reported 8.8 million paying users two years ago).[65] Perhaps for these reasons, the Commission has subjected one-way interconnected VoIP services to the same regulatory requirements as two-way interconnected VoIP services in other contexts, such as TRS funding and more recently the need to pay switched access charges.[66] There is simply no reason now, if there ever was, to distinguish between two-way and one-way interconnected VoIP services for universal service funding purposes, at least when either utilizes the PSTN.

Accordingly, the Commission should act promptly to close the loophole in its existing rules, and subject *all* interconnected VoIP services that utilize the PSTN to direct universal service fund assessment.

d. **Broadband Internet Access Services**

The single most glaring loophole in the current universal service contribution system is the blanket exemption afforded to the providers of broadband Internet access services. The Commission has long recognized that broadband Internet access services include the provision of "telecommunications."[67] However, because the Commission classified broadband Internet access services as "information services," the entire service category has been treated as exempt from universal service contributions.[68] This is true regardless of whether broadband

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65 *FNPRM* at ¶ 62.

66 *Connect America Fund et al.*, WC Docket No. 10-90 *et al.*, Report and Order and Further Notice of Proposed Rulemaking, 26 FCC Rcd 17663, at 18006-7 (2011) ("*USF Distribution/Access Charge Reform Order*").

67 *Appropriate Framework for Broadband Access to the Internet over Wireline Facilities*, CC Docket No. 02-33, Report and Order and NPRM, 20 FCC Rcd, 14853, 14915 (2005) ("*Wireline Broadband Internet Access Service Order").*

68 *Wireline Broadband Internet Access Service Order*, 20 FCC Rcd at 14863-64.

Internet access services are provided by wireline carriers, wireless carriers or cable operators.[69] As a result, it is estimated that over $130 billion in broadband Internet access service revenues will totally avoid universal service assessment this year.[70]

Moreover, the size of this loophole is growing exponentially – it is estimated, for example, that wireless broadband Internet access revenues alone will exceed $140 billion by 2015, more than double the amount of wireless voice revenue.[71] To put these figures in context, it is important to note that the entire revenue base assessable for universal service purposes currently is approximately $67 billion, or approximately half the amount of broadband Internet access revenue that currently is escaping responsibility for universal service funding. Thus, even if only half of interstate broadband Internet access service revenues were assessable, the contribution factor could be cut in half overnight.

Left untouched, this problem will only grow, as the exemption afforded to broadband Internet access services provides a powerful incentive for providers and customers to reallocate revenues from assessable categories to non-assessable broadband Internet access services. For example, Verizon recently announced plans to provide voice and texting services free of charge while boosting the billing rates applicable to the provision of wireless data services.[72] The net result under current universal service contribution rules could be that Verizon's mobile wireless services would *totally* evade any responsibility for universal service

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69 *See, Inquiry Concerning High-Speed Access to Internet Over Cable,* Declaratory Ruling and NPRM, 17 FCC Rcd 4798, 4822 (2002); *Appropriate Regulatory Treatment for Broadband Access to the Internet Over Wireless Networks*, Declaratory Ruling, WT Docket No. 07-53, 22 FCC Rcd 5901 (2007).

70 *See FNPRM* at ¶ 71.

71 *Id.*

72 "A shift at Verizon: Free calls, costlier data," The Washington Post, June 13, 2012 at p. 4.

support – the result of simple strategic pricing strategies rather than any real change in the method of service delivery.[73]

Whether broadband Internet access service ever was properly made totally exempt from responsibility for supporting universal service is highly debatable. However, the exemption has been made completely inequitable by the Commission's recent decision to redirect universal service support to fund the provision of broadband Internet access services.[74] It is nonsensical to deploy scarce universal service funds to subsidize expansion of broadband Internet access services while simultaneously giving the providers of broadband universal Internet access services a "free pass" on contributing any financial support to the universal service program. The time to include these services in the contribution mechanism clearly has come.[75]

Of course, it would be proper to make only the telecommunications transmission component of broadband Internet access services assessable, and continue to permit service providers to treat the information services component of the services as non-assessable. XO submits that revenue for the transmission component could be imputed similar to the MPLS Industry Group proposal, based on a proxy developed by the Commission based on publicly available reasonable rates for comparable transmission services. This would ensure, again, that USF contributions are assessed on a competitively neutral basis at the same level for all providers.

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73 Predictably, AT&T has indicated that it will launch a wireless pricing plan similar to that announced by Verizon. *See*, "Verizon launches 'Share Everything' wireless pricing plans," ETI Views and News, Economics and Technology, Inc. (June 2012).

74 *See generally, USF Distribution/Access Charge Reform Order*.

75 The Commission has asked whether broadband Internet access services should be treated differently for universal service assessment purposes when provided to mass market customers. *See FNPRM* at ¶ 70. The answer is no. Mass market customers of both wireline and wireless voice and basic data services are assessed currently; there is no reason to relieve them of their universal service support responsibility simply because they migrate to functionally equivalent services over a broadband platform.

Implementation of this proposal alone could add approximately $65 billion annually[76] to the assessable revenue base – which would nearly double the base of interstate assessable revenue and, correspondingly, enable the contribution factor to be cut in half. No other single reform could so quickly and easily make universal service funding more sustainable and equitable.

IV. LONG TERM REFORM – OTHER CONTRIBUTION METHODOLOGIES ARE NOT AS ATTRACTIVE NOR AS READY TO IMPLEMENT AS REVENUE REFORM

In this section, XO explains why a revenues-based contribution methodology is preferable and more administratively simple than a numbers-based, connections-based or hybrid methodology.

A. A Modified Revenues-based Assessment System is the Best Way To Implement Universal Service Contribution Reform.

The scores of existing contributors to the universal service fund have dedicated enormous resources into becoming compliant with the existing universal service contribution framework. They have invested heavily in systems and staff as necessary to collect universal service surcharges, report accurately to USAC, remit funds, participate in audits, stay abreast of developments and the like. Replacing the existing revenues-based system with a vastly different contribution mechanism would require all contributors to start over, and make these investments anew; the hardship would fall most acutely on smaller companies who cannot readily afford to revamp billing systems or retrain staff simply to comply with changing regulatory requirements. Thus, the Commission should make the minimum changes to the existing contribution framework necessary to ensure the sustainability of the fund and competitive equity.

76 Since all broadband Internet access services are classified as "interstate" for jurisdictional purposes, assessment of the telecommunications component of broadband Internet access services would be particularly accretive to the interstate universal service revenue base.

Fortunately, radical surgery is not required to accomplish the goals of contribution reform. The existing revenues-based assessment system can do the job nicely if it simply is updated to permit assessment of all services that entail the provision of telecommunications and benefit from access to the PSTN. Based on the preceding discussion, it is evident that the Commission can and should increase the list of assessable services substantially. Even allowing for reasonable allocations that permit revenue attributable strictly to information services components to remain non-assessable, it is evident that the suggested reforms likely would add $100 billion or more of revenue annually to the base of assessable revenues. This would permit the quarterly contribution factor to be reduced by *approximately 2/3*. Reducing the contribution factor from an average of 17 percent to-date in 2012 to something closer to 5 percent would quickly and easily cure many of the biggest problems with the current universal service system. Competitive arbitrage would be greatly reduced – thereby making the system both more fair and stable – without having to develop and implement an entirely new and incredibly complex system.

Notably, timing is of the essence. A contribution factor nearing 16 percent – and applied unevenly among competing services – is unsustainable even in the short term. Thus, which reform can be implemented most expeditiously is a critical factor. The proposed expansion of assessable services can be implemented with relative ease during 2013. All that is required is for the rules to make clear that revenue from the additional services must be reported as assessable on the current Form 499-A, and give service providers a fair opportunity to begin collecting universal services surcharges from end users that purchase the affected services. History suggests that this can be accomplished within approximately six months.[77] By contrast,

[77] Market evidence can be gleaned from the recent addition of conference calling services to the list of assessable revenues. Audio bridging providers were able to register and begin

implementing a new numbers- or connections-based system would require extensive additional rulemaking, creation of entirely new forms and reporting systems, and extensive modification of carrier billing systems to permit recovery from customers – changes that could take years to devise and implement.

Thus, the existing revenues-based system needs to be fixed, not replaced.

B. Neither A Numbers-Based Nor Connections-Based Contribution System Would Improve The Existing System Materially.

As discussed above, there is no compelling rationale for the Commission to abandon the current contribution scheme. Instead, the revenues methodology can achieve the Commission's goals by broadening its base of assessable services to accommodate service migrations since the system was put in place. Equally important, none of the alternative proposals ensure that providers of interstate telecommunications services make equitable and nondiscriminatory contributions to USF, as required by Section 254. Whether the Commission considers a telephone numbers-based, connections-based or a hybrid methodology, each alternative would require carriers to implement costly new tracking and billing mechanisms, and none would simplify the contributions system over the existing revenues methodology.

1. Numbers-based methodology

A telephone numbers-based methodology presents numerous challenges. Despite the superficial allure of its alleged simplicity, a numbers-based methodology is not forward-looking. Such an approach does not account for the myriad non-traditional uses of numbering resources made by service providers today and in the future. For example, devices that provide

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reporting revenues within 6 months of the Commission's decision to add conference calling to the list of assessable services. *Request for Review by InterCall, Inc. of Decision of the Universal Service Administrator*, Order, 23 FCC Rcd 10731 (2008) (June 2008 order directing audio bridging providers to contribute to the USF as of October 1, 2008).

machine-to-machine connections, such as Kindle and Nook e-readers, gaming consoles, and smart grid networks, often utilize numbering resources even though they provide no voice component. These devices provide ongoing services utilizing telecommunications networks but require no ongoing monthly fee or billing relationship with a telecommunications provider. Consequently, as noted in the *FNPRM*, many of these providers argue for exceptions from numbers-based assessments for their uses or their services.[78] Such exceptions would introduce a new level of complexity to the supposedly simple number-based assessments. Service providers would have to implement procedures to track number assignments by types of use, and USAC and the Commission would have to audit and verify uses in order to implement the exemptions.

Conversely, a numbers-based methodology fails to account for the ways telecommunications may be provided in the future. Some VoIP services mimic traditional telephony but route calls utilizing ENUM databases rather than via the PSTN using numbering resources. Failure to include such uses would potentially lead to inequitable exemptions for these providers under a numbers-based system. Attempts to define and include ENUM resources would add a layer of complexity that the rules are ill-equipped to handle.

In addition, companies continue to develop innovative new products and services that minimize the use of the PSTN (and, in turn, numbering resources). The Commission should not adopt policies that would stifle such innovative services or encourage arbitrage opportunities. A numbers-based methodology for federal USF contributions could lead to gaming of the system as carriers modify services to unnecessarily avoid or hide the use of numbers. While no one can predict every future potential use of numbering resources, we do know that the state of the industry is not static and will constantly be moving forward.

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78 *FNPRM* at ¶¶ 312-15.

Further, the connection between telephone number assignment and the provision of telecommunications is tenuous at best. Increasingly, numbering resources are being used for services other than telecommunications, while on the other hand, the provision of VoIP services similar to traditional telephony are reducing their use numbering resources. Therefore, there is little nexus between assignment of telephone numbers and usage of interstate telecommunications. Since use of numbers does not reflect usage of interstate telecommunications, a numbers-based approach risks placing a disproportionate responsibility for USF contribution upon relatively small users of interstate telecommunications. Prominent examples include government agencies, military bases, universities, and hospitals, who use thousands of numbers but who often have relatively low usage of interstate telecommunications per line. Granting exceptions for these *de minimis* users – in addition to other users also seeking exemptions – would complicate administration of the fund as well as shrink the base for contributions. By contrast, some users consume large volumes of interstate telecommunications over connections that have no associated telephone numbers (VoIP services with no telephone number assigned, for example) and thus avoid contributing to USF entirely under a numbers-based approach.

A numbers-based approach also sets up a serious jurisdictional conflict. Many lines with numbers assigned to them are used exclusively to purchase local exchange or other purely intrastate telecommunications services. Without some complex administrative scheme to cope with the problem, a numbers-based approach could unlawfully assess federal USF for purely intrastate services. Even where a line is not used exclusively for intrastate telecommunications, a flat-rate contribution mechanism cannot properly account for a customer's relative consumption of interstate versus intrastate telecommunications.

2. <u>Connections-based methodology</u>

A connections-based system suffers from many of the same pitfalls as a numbers-based system because of the limited nexus between connection speeds and telecommunications usage and the complexities in identifying an assessable connection and the various capacities or speeds of circuits.

Importantly, there is little correlation between connection capacity or speeds and usage of telecommunications services. The capacity or speed of a particular circuit merely identifies the amount of bandwidth that may be available for usage. The industry trend is moving toward offering customers burstable services with a maximum capacity and no monthly usage commitment or recurring charges. Instead, the customer pays entirely based on its monthly usage, regardless of the overall circuit capacity, allowing for fluctuations in usage each month. For these services, revenue collected is the best indicator of telecommunications usage. Additionally, customers often purchase excess bandwidth for backup or future growth so that capacity or speed alone does not accurately reflect their use of particular circuits or services. Thus, assessing USF based on available bandwidth improperly taxes spare capacity and could lead to poor network management practices.

XO disagrees that a connections-based system would be more administratively simple or provide a more stable contribution base. Rather, implementation of a connections-based system would impose considerable costs without commensurate benefit. Each of the Commission's proposed definitions of "connection" would lead to inequitable assessment on providers of comparable services. For example, if a "connection" were defined as the provision of a facility or line with access to an assessable service, any provider of over-the-top VoIP services could be exempted from contribution. This would be highly inequitable and lead to a dwindling contribution base, especially considering the increased use of VoIP services in lieu of traditional wireline voice services. If a "connection" were defined as an assessable service, it would be subject to the same discrepancies in interpretation as the classifications of assessable services under the revenue-based system, thereby offering no benefit over the current system.

Additionally, implementation would require significant expense and modification to billing systems to properly track circuit capacity by customer and bill for recovery of USF contributions. For example, XO's multiple billing systems do not track circuit capacity on a real-time basis for each and every circuit provided to each and every customer. While XO is able to track and report the capacities of circuits provided on an aggregate basis for certain reporting, this data is not compiled in its billing systems in such a way to allow for accurate assessment and recovery from end users. Moreover, implementing a connections-based system for assessing federal USF while state USF funds remain revenue-based would be particularly complicated, leading to both gaps and double counting of services for assessment. There is no reason for the Commission to undertake a new contribution methodology without clear benefits over the current revenue-based system.

3. Hybrid methodologies

A hybrid system cures none of the deficiencies of a purely numbers-based or connections-based system. Rather than provide a simpler, more cost-effective means of assessing contributions from service providers, hybrid contribution mechanisms are more complex and expensive to administer than the current revenues-based contribution mechanism. As a result, hybrid systems represent a "worst of both worlds" outcome rather than a correction of the limitations of one system over another.

A hybrid mechanism would create and require contributors to follow complex and sometimes ambiguous distinctions between types of assessable services, number resources <u>and</u>

connections. Carriers would have to simultaneously maintain processes to distinguish residential/wireless versus business customers, entities covered by Section 254 of the Act versus entities not covered by Section 254, North American Numbering Plan ("NANP") numbers versus NANP number equivalents, and number (or number-equivalent)-based services versus non-number based services. All the while, a carrier would not be relieved of any distinctions required under each of the methodologies that comprise the hybrid system.

As a result, a hybrid system would require expensive modifications – times two – to billing systems, accounting practices, and information technology resources to calculate and recover contributions based on two methodologies. For example, a numbers/revenues hybrid system would require carriers to maintain current revenue tracking systems while adopting new tracking mechanisms to ascertain whether a number is assigned to a residential or business customer, to report numbering usage for universal service fund purposes, and to calculate and recover contributions based upon the type of end user. Similarly, a hybrid numbers/connections contribution mechanism would require carriers, at a minimum, to develop the ability to track whether a number is assigned to a residential or business customer, to track and report numbering usage and the speed of the connection that provides service to a customer, and to modify billing, accounting practices, and information technology resources to calculate and recover contributions based upon the type of end user. Because of their complexity and ambiguity, hybrid proposals increase implementation, administrative and compliance burdens, create additional opportunities for arbitrage, and make compliance audits by regulatory authorities much more difficult and expensive. These detriments far outweigh any benefits they may offer and would make the contribution mechanism less stable and predictable than the current revenues based system.

V. <u>THE FCC SHOULD MAKE USF ADMINISTRATION MORE EFFICIENT AND PREDICTABLE</u>

A. <u>The FCC Should Not Imbue The Form 499-A Instructions With The Force Of Rules.</u>

The *FNPRM* seeks comment on whether it should modify the process by which the Form 499-A and the accompanying Instructions are revised.[79] XO supports procedural changes that will provide advance notice of revisions to the Instructions and provide an opportunity for public comment on the revisions. However, the Commission should not convert the Instructions' guidance into binding FCC rules. The underlying FCC Orders, duly adopted pursuant to the requirements of the Administrative Procedure Act, should remain as the only source of binding obligations for contributors.

As the *FNPRM* notes, the Wireline Competition Bureau currently publishes updated instructions for the Form 499-A annually pursuant to delegated authority. The authority delegated to the Wireline Competition Bureau is carefully limited to non-substantive changes to the rules, however. In its 1999 *Carrier Contribution Reporting Requirements Order*, the Commission delegated limited authority to the then-Common Carrier Bureau to modify Commission reporting forms.[80] Specifically, the Commission explained the limitations on the authority delegated to the Bureau as follows:

> These delegations extend to administrative aspects of the requirements, e.g., where and when worksheets are filed, incorporating edits to reflect Commission changes to the substance of the mechanisms, and other similar details. . . . We reaffirm that this delegation extends only to making changes to the

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79 *FNPRM* at ¶¶ 344-49.

80 *1998 Biennial Regulatory Review – Streamlined Contributor Reporting Requirements Associated with Administration of Telecommunications Relay Services, North American Numbering Plan, Local Number Portability, and Universal Service Support Mechanisms*, 14 FCC Rcd 16602, 16621, ¶¶39-40 (1999) ("*Carrier Contribution Reporting Requirements Order*").

administrative aspects of the reporting requirements, not to the substance of the underlying programs.[81]

As a result of this limited delegation, the Wireline Competition Bureau is not permitted to make substantive changes and is not permitted to adopt binding rules for contributor reporting obligations. Thus, the Form 499-A Instructions are guidance to contributors, which the Commission and the Bureau have affirmed previously.[82]

XO supports greater transparency and greater public input into the development of this guidance from the Bureau. For this limited purpose, XO would support the proposal to require the Wireline Competition Bureau to release proposed revisions to the Form 499-A Instructions and to seek public comment on the revisions.[83] But – and this is critical – this public input should not imbue the Instructions with greater legal significance than they enjoy today. That is, in authorizing public input into the revisions, the Commission should not modify the limited delegation of authority given to the Wireline Competition Bureau. The Bureau should continue to be limited to modifying the "administrative aspects" of the USF reporting requirements, not to make substantive changes to the program.

This distinction is key. Several pending appeals require interpretation of complex FCC decisions, sometimes enacted over a period of years. For example, several pending appeals

81 *Carrier Contribution Reporting Requirements Order*, ¶¶39-40.

82 *Request for Review of Decision of the Universal Service Administrator by Global Crossing Bandwidth, Inc.*, Order, 24 FCC Rcd 10824 (2009) ("the instructions are indeed guidance from the Commission"); *In re Universal Service Contribution Methodology; Request for Review of Decision of the Universal Service Administrator by Network Enhanced Telecom, LLP*, 25 FCC Rcd 14533 (WCB 2010) ("while the Commission does not dictate what procedures a carrier must implement to meet the 'reasonable expectation' standard, the agency has provided guidance in the FCC Form 499-A instructions to assist wholesale carriers").

83 *See FNPRM* at ¶ 346.

address the issue of whether particular private line services are interstate or intrastate in nature.[84] The rules for determining the jurisdiction of private lines were first adopted in the 1980s as part of the cost separations process for dominant local exchange carriers as a means to allocate certain special access or private line costs to the intrastate or the interstate jurisdictions when such facilities carry both intrastate and interstate traffic. The Part 36 rules underlying separations have been modified periodically over the last decades through careful processes that included input from a wide variety of federal and state interests, affected carriers and the public. These rules are distilled into a single sentence in the 2012 Form 499-A Instructions, stating that "if over ten percent of the traffic carried over a private line or WATS line is interstate, then the revenues and costs generated by the entire line are classified as interstate."[85] As guidance, this one-sentence shorthand may be sufficient, and, if necessary, could be supplemented by adjudications involving specific appeals and specific circumstances. If the Form 499-A Instructions were to become rules, however, the entire two decades of Separations orders would have to be distilled fully and accurately into the Instructions.

Such a process for distilling all FCC Orders into concise and binding re-statements is unrealistic. XO doubts that the public notice process could bear the weight of such a task. Either the result would be binding rules that fail to capture the entirety of the FCC orders

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84 *See Request for Review by Madison River Communications, LLC of Decision of Universal Service Administrator*, Request for Review, WC Docket No. 06-122 (filed Dec. 12, 2008) ("Madison River Request for Review"); *XO Communications Services, Inc. Request for Review of Decision of the Universal Service Administrator*, Request for Review of Decision of the Universal Service Administrator, WC Docket No. 06-122 (filed Dec. 29, 2010) ("XOCS Request for Review"); *Request for Review of PaeTec Communications, Inc. of Universal Service Administrator Decision*, Request for Review of PaeTec Communications, Inc. of Universal service Administrator Decision, WC Docket No. 06-122 (filed April 3, 2012) ("PaeTec Request for Review").

85 2012 Form 499-A Instructions, at pp. 22-23.

or the entire process would rapidly become a quagmire as interested parties re-fight battles decided in separate proceedings.

For these reasons, XO recommends that, regardless of the process improvements adopted for creating the Form 499-A Instructions, the Commission affirm that it is not modifying the limited delegation given to the Bureau to modify the administrative aspects of the revenue reporting worksheets. The Commission can welcome greater public input into the guidance provided by the Instructions, but it should clearly and unequivocally affirm that the Instructions remain just that – guidance, not binding rules. With such clarifications, it will be clear to USAC that it cannot apply the Instructions as if they were rules. Instead, the underlying FCC orders are the only applicable source of binding requirements. If application of those orders is not clear, then USAC is to seek further guidance from the FCC.[86]

B. <u>The FCC Should Move To An Annual USF Contribution Factor.</u>

For the reasons explained in section II.D., above, an annual contribution factor is preferable to the current quarterly contribution factor. A move to an annual contribution factor will be easier to administer for service providers and USAC alike. In addition, an annual contribution factor will produce a more stable and predictable contribution factor for end users than does the current quarterly contribution factor. The quarterly factor is too influenced by temporary swings in revenue due to seasonality and other factors. Therefore, XO supports modifying the contribution rules to adopt an annual USF contribution factor.

C. <u>The FCC Should Reject The Pay And Dispute Proposal In The NPRM.</u>

The *FNPRM* proposes a rule that would require USF contributors to make full payment of the amount billed by USAC, even where such amounts are disputed or subject to an

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[86] *See* 47 C.F.R. § 54.702(c).

appeal.[87] Specifically, the so-called "pay and dispute" rule would require a contributor to pay the full amount invoiced, or be assessed late fees, interest charges and penalties. Such fees, interest and penalties would apply even if an appeal were ultimately granted by the FCC, except if the disputed charges are the result of "clear error by the Administrator."

XO strongly opposes this proposed rule in the context of appeals or other proceedings where a contributor disputes a USAC decision because the proposed rule could impose a significant financial hardship on contributors. In an audit context, proposed revisions by USAC can involve large amounts of revenue and, especially at current USF contribution factors, significant USF contribution amounts. By definition, moreover, these will be revenues that the contributor did not initially classify as assessable, and therefore, the contributor will not have collected USF contribution recovery fees from end users. The contribution obligation could run in the millions of dollars even for smaller carriers.

Requiring an entity to pay the disputed amount in order to appeal a USAC decision shifts too much of the burden to contributors. Under the proposed rule, even if the carrier ultimately is successful and USAC's position is reversed, the filer would be responsible for substantial late fees, interest and penalties on amounts that the Commission determines were not properly due in the first place. Contributors that pay the disputed amounts prior to appeal would suffer the loss of capital and experience potential cash flow troubles while pursuing a meritorious appeal. Such contributors, if successful, presumably would receive a refund of the overpayments, but would in essence be forced to loan these amounts interest free to the Universal Service Fund. Such a position is fundamentally unfair to contributors.

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[87] *FNPRM* at ¶ 363 (proposing "pay and dispute" rule).

Moreover, a "pay and dispute" policy runs contrary to the way that industry participants typically treat disputes involving payment. Under many contractual arrangements and carrier tariffs, customers are obligated only to pay the undisputed portions of invoices while a dispute is pending. If the customer ultimately is successful with the dispute, the disputed bill is revised and no further amounts are due. If the customer dispute is denied, however, the customer becomes liable both for the disputed amount and any interest or penalties on the unpaid amount. This industry solution is much more balanced than the Commission's "pay and dispute" proposal and is more equitable both to the billed entity (the contributor in the USF context) and the billing party (the Fund).

The better approach would be for the Commission to follow the industry standard practice in the case of USF appeals and disputes. Payment of disputed amounts should not be required while an appeal is pending. If an appeal is denied, however, the contributor may be liable for the disputed amount, plus any interest or penalties applicable to the unpaid amount.

Finally, the proposed "pay and dispute" rule conflicts with current procedures under the Debt Collection Improvement Act (DCIA) and the Commission's "red-light" rules. Currently, if a contributor has appealed an assessment, USAC invoices the contributor for the challenged amounts, including interest. USAC suspends DCIA referrals to the Commission while the appeal is pending, however. As a result, no appeal causes a contributor to face debt collection referrals under the DCIA procedures and no appeal results in a contributor being placed on "red light" status under the FCC rules. Codification of a "pay and dispute" rule would undermine this policy and force contributors to pay disputed USF assessments simply to avoid the onerous consequences of the DCIA rules. Rather than adopting the "pay and dispute" rule, the Commission should codify this existing USAC policy instead. That is, the rules should instruct USAC not to refer disputed assessments under the DCIA so long as a contributor's appeal is pending.

D. The FCC Should Make USF Appeals More Predictable.

Any improvement to the administration of the contribution system must also address contributor appeals of USAC decisions. Appeals of USAC decisions play an important role in clarifying USF rules and in applying the rules to new situations. Prompt resolution of these issues is vital to ensure that funding of the programs remains sufficient and that administration of universal service continues to be equitable and non-discriminatory. To achieve these goals, the Commission should revise its rules for consideration of contributor appeals to establish a reasonable time period for resolution of the appeal, backed by meaningful consequences that provide contributors with needed certainty concerning their contribution obligations.

The Commission already has a rule in place to govern appeals of USAC decisions. Section 54.724 of the Commission's rules creates a 90-day deadline for the consideration a request for review of a USAC decision, with an opportunity to extend the deadline by an additional 90 days.[88] When it adopted this deadline, the Commission expressed confidence that the 90-day period would "provide an adequate opportunity for review, in most cases," and that the opportunity to extend review would be sufficient for the remainder of cases.[89] In the context of contributor appeals of USF assessments, however, it is apparent that

88 47 C.F.R. § 54.724. Subsections (a) and (b) of 54.724 establish 90-day deadlines for appeals before the Bureau and the Commission, respectively. These deadlines may be extended by the Bureau or Commission for a period of up to an additional 90 days. *Id.*

89 *Changes to the Board of Directors of the National Exchange Carrier Association, Inc., Federal-State Joint Board on Universal Service,* Third Report and Order and Fourth Order on Reconsideration in CC Docket No. 97-21, Eighth Order on Reconsideration in CC Docket No. 96-45, 13 FCC Rcd 25058, 25093-94, ¶ 70 (1998) ("*Eighth Order on Reconsideration*").

the Commission's assumptions were overly optimistic. Contributor appeals routinely take longer than the 90 days to resolve. Indeed, it is not unusual for a contributor appeal to be pending for two years or more before a decision is rendered. With respect to contributor appeals at least, the FCC should replace its 90-day deadline with a more realistic timeline that allows prompt but full consideration of the appeal.

Although XO supports an extension of the overly optimistic 90-day deadline for contributor appeals, appeals should be resolved promptly. Having appeals languish for years is detrimental to the petitioning contributor and unfair to the industry. For the contributor, the pendency of an appeal presents a Hobson's choice: the carrier either must continue to follow the interpretation it believes is correct, at the potential expense of additional USF liability, or it must alter its practices and assess USF consistent with the USAC interpretation but in a manner that the carrier contends is wrong. In either event, the length of time that an appeal is pending extends and exacerbates the damage from this choice. For the industry, other contributors are not able to obtain additional guidance as to the proper interpretation of the rules. This is especially troublesome when the petitioning contributor is advancing an interpretation that subjects less revenue to USF assessments than the way other industry participants have treated the revenue. The longer the appeal is pending, the longer the industry lacks guidance and, potentially, the longer the petitioning contributor enjoys a competitive advantage in the form of lower USF obligations for its end users compared to end users of other contributors.

XO believes that a one-year deadline for resolution of contributor appeals properly balances the Commission's need for time to review appeals and the industry's need for a resolution. A one-year deadline is consistent with the Commission's time period for resolution of forbearance petitions, petitions which can sometimes raise policy issues much broader than those raised in an appeal.[90] The one-year deadline is longer than the period provided for certain formal complaints[91] and the time that was provided for review of BOC Section 271 petitions.[92] A one-year time period for resolution should be more than sufficient to address the issues raised in a contributor appeal.

In order to encourage Commission action within the time period, the one-year deadline should be accompanied by a "deemed granted" provision. If the Commission fails to issue an order in response to the appeal within one-year, then the petitioner's appeal should be deemed to have been granted.[93] As a result, the petitioner would not be obligated to pay the additional USF at issue in the appeal. However, this provision would be limited to the petitioner and to the specific time period at issue in the audit or other USAC decision. That is, the "deemed granted" provision would have effect only with respect to that petitioner and that specific time period at issue. It would not affect other contributors, and, with respect to the petitioner, would not limit the ability of USAC or the FCC to examine future time periods.[94]

Thus, this proposal would create a distinction between precedent-setting resolutions and non-precedential resolutions of USF appeals. If the FCC acts on an appeal, the

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90 47 U.S.C. § 160(c).

91 *Id*. § 208(b)(1) (providing a 5-month deadline).

92 *Id.* § 271(d)(3) (providing a 90-day deadline).

93 *Cf.* 47 U.S.C. § 160(c).

94 When the Commission first adopted Section 54.724, it included a provision providing for default consequences in the event of Bureau inaction. In the original version of Section 54.724, if an appeal properly before the Common Carrier Bureau was not acted upon within 90 days, then USAC's decision would be deemed to be upheld. *Eighth Order on Reconsideration*, 13 FCC Rcd at 25096, ¶ 74. However, the rule did not provide similar consequences for appeals properly before the Commission (*i.e.*, those appeals raising novel issues of law or policy). Because it was too difficult for petitioners to determine whether an appeal would be addressed by the Bureau or by the Commission, the FCC eliminated the consequences of the Bureau's non-action. *Federal-State Joint Board on Universal Service (Changes to the Board of Directors of the National Exchange Carrier Association, Inc.)*, Order, 15 FCC Rcd 9336 (2000). XO submits that the presumption in favor of USAC's decision was inconsistent with the *de novo* review of USF appeals, and therefore such a presumption was incorrect in the first place.

Commission's order is binding, and it would have the same effect as any other order by the Commission, but the Commission's inaction would be non-binding and non-precedential.

E. <u>The FCC Should Adopt Procedures For USAC Contributor Audits.</u>

The *FNPRM* also seeks comment on processes and procedures that USAC could implement to make the contributor audit process more efficient.[95] XO has two suggestions for procedural changes that will make the audit process more transparent and more efficient.

Transparency. XO proposes that USAC be required to prepare an audit summary for each contributor audit that it completes. This summary should identify the issue(s) raised, USAC's analysis of the issue, including its application of the FCC rules to the issue, and should state in general terms the finding made by USAC. Such Audit Summaries should not identify the contributor audited by name, and should not contain any information which is confidential to the contributor, including the amount of revenue at issue.

The benefit of these Audit Summaries is to provide the industry notice of USAC decisions so that they may have a better understanding of how the USF rules are being applied. Therefore, these Audit Summaries should be made publicly available by posting them on USAC's website or the Commission's website. Posting of Audit Summaries would make the USAC contributor audit function more transparent, enable the industry and the FCC to be aware of patterns in USF controversies and promote the goal of a more uniform application of the USF rules by all contributors. XO recommends that the FCC order USAC to produce such summaries for each contributor audit.[96]

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95 *FNPRM* at ¶ 371.

96 XO notes that the FCC Inspector General posts redacted versions of the audit report itself when it conducts contributor audits. *See, e.g.*, Final Audit Report, Associated Network Partners, Inc. (Mar. 22, 2011), available at http://transition.fcc.gov/oig/ANPI_Final_Report_03_22_11_Redacted.pdf (last visited

Fair opportunity. In addition, the FCC should codify minimal procedural rules for USAC to follow in the conduct of contributor audits. Currently, USAC follows a procedure that, with one minor exception, XO believes is generally sufficient. Currently, USAC initiates an audit by sending the contributing carrier a package describing the audit scope and time period (typically, one Form 499-A), and requesting basic information to conduct the audit. Contributors are given a reasonable time period to provide the information. Afterwards, USAC conducts an Entrance Conference followed by on-site field work. After completion of field work, USAC provides draft audit findings to the contributor, and the contributor is given an opportunity to respond, in writing to the draft findings. The contributor's written response is included verbatim in the final audit report. After further review by USAC's Financial Operations group and by USAC's Management, the audit report is presented to the USAC Board of Directors for consideration. The FCC should mandate use of this process in order to ensure a fair opportunity for contributors to have input into the audit process.

XO recommends one improvement to the current process in order to ensure that contributors have a meaningful opportunity to review and respond to the USAC proposed findings, prior to adoption by the USAC Board. As described above, the current USAC procedure affords the contributor an opportunity only to review the initial draft audit findings. After submission of its response to the draft audit findings, the contributor does not have any insight into USAC's consideration of the audit until the audit is adopted by the USAC Board. The contributor is not given further notice of USAC's consideration during the audit process itself, including any opportunity to review modifications made during USAC's senior level review of the contributor response. XO proposes that, in addition to review of the initial draft

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July 6, 2012). XO believes that this level of detail is not required, but would support this practice if followed by USAC as well.

audit findings, contributors also be provided with a copy of the proposed final audit report two weeks before it is presented to the USAC Board. Contributors should then be given an opportunity to address the USAC Board, either in writing or in person to respond to the proposed final audit report. This further opportunity would be akin to a closing argument in a trial, and, accordingly, should be brief in length and summary in nature. The FCC could set reasonable time limits or page limits on this response.

VI. THE COMMISSION SHOULD NOT MODIFY ITS RULES FOR RECOVERY OF USF CONTRIBUTIONS FROM END USERS

In the final section of the *FNPRM*, the Commission seeks comment on proposals to modify the way in which universal service contribution charges are passed through to their customers. XO opposes the changes discussed in this section. Generally, XO does not believe that there is a need to change the existing regulations relating to recovery of USF contribution charges from end users. The current system is working well and, to XO's knowledge, has not generated consumer confusion or complaints.

A. Line-Item Recovery Of USF Contributions Must Be Permitted.

On particularly troublesome area of overreach in this section is the *FNPRM*'s proposal to eliminate line-item USF surcharges on consumer bills.[97] XO opposes any proposal to prohibit contributors from recovering their USF contribution costs through an end user line-item surcharge.

At the outset, XO notes that the *FNPRM* offers no explanation of the purported need for such a rule. The *FNPRM* does not assert that there is any consumer harm caused by line-item surcharges, nor does it explain the benefit of such a rule. Without any need for or benefit from the rule, the Commission should abandon the proposal.

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[97] *FNPRM* at ¶ 394.

This is particularly true with respect to a proposed limit on carrier discretion in billing customers. The FCC's Truth-in-Billing rules already afford carriers maximum flexibility in billing customers, limited only by common sense principles that bills be truthful, non-misleading and clearly presented to customers.[98] These limited regulations properly balance consumer protection with constitutional limitations on the FCC's discretion. Indeed, any limit on a carrier's ability to truthfully identify a charge as derived from the federal universal service program would raise significant First Amendment concerns.[99] The Commission should not wade into this troublesome area when no record is established for the proposal.

B. The Proposal To Establish "Trust Funds" For USF Contributions Is Burdensome And Unnecessary.

XO also opposes the *FNPRM*'s proposal to require contributors to segregate USF contribution recovery charges into dedicated trust accounts.[100] This rule is proposed in order to increase collection of USF contributions from carriers in cases of insolvency or financial distress.[101] However, the proposed rule would impose significant burdens on thousands of contributors in an effort to address what appears to be an extremely minor problem.

The *FNPRM* states that from 2001 through 2011, the Fund was unable to collect in bankruptcy cases approximately $80 million in revenues that carriers had recovered from end

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98 *See* 47 C.F.R. §§ 64.2400, 64.2401.

99 Many courts have overturned efforts to ban or limit line-item charges on First Amendment grounds. *See, e.g., BellSouth Telecommunications, Inc. v. Farris*, 542 F.3d 499 (6th Cir. 2008) (Kentucky statute prohibiting telecommunications carriers from identifying new tax on consumers' bills is unconstitutional); *Bloom v. O-Brien*, 841 F.Supp. 277 (D. Minn. 1993) (granting injunction against Minnesota statute prohibiting providers from itemizing gross revenue tax on patient bills); *cf. Rubin v. Coors Brewing Co.*, 514 U.S. 476 (1995) (statute prohibiting beer labels from displaying alcohol content violates First Amendment).

100 *FNPRM* at ¶ 400.

101 *Id.*

users as USF contribution recovery surcharges.[102] In context, however, this number is extremely small compared to the Universal Service Fund as a whole. Elsewhere, the *FNPRM* reports that the size of the Universal Service Fund grew from $4.5 billion annually in 2000 to $8.1 billion in 2011.[103] A loss of $80 million over ten years represents only one-one-hundredth of one percent (0.0001 or 0.01%) of the 2011 Fund's size. Such a loss can easily be accounted for through the customary bad debt reserve already included within USAC's USF projections. There is no need, therefore, for any additional measure to ensure the recovery of contributions in the situations identified by the *FNPRM*.

Moreover, the costs of any solution to this problem would far outweigh its potential benefits. The *FNPRM* does not identify the number of contributor bankruptcies that produced the $80 million figure cited as a loss, but it is likely that this number is well below 100 proceedings. The proposed trust fund solution, by contrast, would apply to all contributors, not just those experiencing financial distress. There are approximately 2,900 current contributors to the Fund, and another 3,100 providers that would otherwise to be contributors but for the *de minimis* exemption.[104] Imposition of a trust fund obligation on these entities would be extremely costly across the industry as a whole. Implementation costs and on-going carrying costs would far exceed the $80 million figure cited as a loss over a ten-year period. Because the costs so overwhelmingly would outweigh the benefits, the Commission should not adopt the trust fund proposal.

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102 *Id.* at ¶ 399.

103 *Id.* at ¶ 20. Demand for 2012 appears likely to top $9 billion.

104 *Id.* at ¶ 9.

VII. CONCLUSION

XO compliments the Commission for a thorough and much-needed reexamination of the USF contribution system. For the reasons explained above, retention of the existing revenues-based USF contribution methodology and a broadening of the USF revenue base is the best means to make the Fund more stable, predictable and equitable. XO accordingly urges the Commission to act swiftly to reform the contribution system as described in these comments.

Respectfully submitted,

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